

**ST 07-3**

**Tax Type: Sales Tax**

**Issue: Exemption From Tax (Charitable or Other Exempt Types)**

**STATE OF ILLINOIS  
DEPARTMENT OF REVENUE  
OFFICE OF ADMINISTRATIVE HEARINGS  
SPRINGFIELD, ILLINOIS**

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**THE DEPARTMENT OF REVENUE  
OF THE STATE OF ILLINOIS**

**v.**

***XYZ CLUB***

**Taxpayer**

**Docket # 06-ST-0000**

**Claim for Exemption**

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**RECOMMENDATION FOR DISPOSITION**

Appearances: Kent Steinkamp, Special Assistant Attorney General, for the Department of Revenue of the State of Illinois.<sup>1</sup>

Synopsis:

*XYZ Club* (“taxpayer”) applied to the Department of Revenue (“Department”) for an exemption identification number so that it could purchase tangible personal property at retail free from the imposition of use and retailers’ occupation taxes. The Department denied the taxpayer’s request, and the taxpayer timely protested the denial. An evidentiary hearing was held during which the sole issue presented was whether the taxpayer is organized exclusively for charitable purposes under section 3-5(4) of the Use

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<sup>1</sup> The taxpayer was not represented by an attorney. *John Doe* and Jim Doe, who are members of the organization, appeared for the taxpayer.

Tax Act (35 ILCS 105/3-5(4)) and section 2-5(11) of the Retailers' Occupation Tax Act (35 ILCS 120/2-5(11)). The Department contends that the primary purpose of the taxpayer's organization is not charitable. After reviewing the record, it is recommended that the Department's decision be affirmed.

FINDINGS OF FACT:

1. The taxpayer is an Illinois not-for-profit corporation. (Taxpayer Ex. A)
2. The taxpayer is one of the subordinate clubs existing under a charter of affiliation legally granted by the National Association of XYZ Clubs. (Taxpayer Ex. C)
3. The taxpayer's by-laws state that it is organized to operate exclusively for charitable, scientific, literacy or educational purposes. (Taxpayer Ex. C)
4. The taxpayer's by-laws also state that its objectives are (1) to foster fellowship among its members; (2) to foster cooperation among its members; (3) to foster fellowship and cooperation with and among other civic bodies; (4) to create an interest in all public welfare; (5) to stimulate the desire of every member of the club to be of service to their community and to society in general; and (6) to make its own constitution, bylaws, rules and regulations for the government of the club. (Taxpayer Ex. C)
5. The taxpayer is a service club that has four classes of membership: active, honorary, senior, and life. Active membership is granted to those who are selected by the club to be members. Any current member may propose a new member for the club. The proposal must be submitted in writing to the Board of Governors, and final approval of a proposed member is vested exclusively in the Board. (Taxpayer Ex. C)

6. Each new member must pay a membership fee, which is currently \$45, and must serve a probationary period for the first twelve months of membership. (Taxpayer Ex. C; Tr. pp. 16-17)
7. Honorary membership may be conferred upon citizens of the United States who have rendered an exceptional public service or exceptional service to the club, and through that service have made themselves qualified for the honor. (Taxpayer Ex. C)
8. Senior membership may be granted to a member who has been a member for at least 10 years and is 40 years of age. Honorary and senior members have voting privileges but are not eligible to hold any elective office in the club. They may attend all functions and be retained on the mailing list, and they pay only for luncheon meetings that they attend. (Taxpayer Ex. C)
9. Life membership may be granted to an active member of the club in good standing who pays a fee determined by the national Board of Directors to the National Office. (Taxpayer Ex. C)
10. The taxpayer's Board of Governors has nine members who govern and control the affairs of the club. The taxpayer also has officers that include President, Vice President, Secretary, Treasurer, and Sergeant-at-Arms. The President, Secretary, and Treasurer may be compensated for their services at an amount that is determined by the Board of Governors. (Taxpayer Ex. C)
11. The taxpayer has luncheon meetings for its members twice a month. It also has Board meetings twice a month, special events, and other get-togethers throughout the year. (Tr. p. 18)

12. In addition to having lunch, usually a speaker provides a presentation at the luncheon meetings. (Tr. p. 19)
13. The taxpayer's largest special event is selling food, beer, and refreshments at a fair. The taxpayer is also in charge of the parking at the fair. The taxpayer's members, as well as other volunteers and charitable organizations, work at the event. (Tr. p. 19)
14. Another special event that the taxpayer sponsors is a golf outing for United Cerebral Palsy. Every net dollar from the event goes to the charity. (Tr. p. 32)
15. The taxpayer's other events include an annual Halloween party for the Boys and Girls Club, a Christmas party for the taxpayer's members, and "social hours." (Tr. p. 21)
16. The Board of Governors adopts a schedule of dues that include monthly chapter dues, a summer assessment, and such other assessments that are needed to meet the club's obligations. The dues also include the per capita tax payable to the National Association, the annual subscription payment for a National Publication and the per capita tax payable to the District Association. (Taxpayer Ex. C)
17. Members are charged for the actual cost of the luncheons, parties or social events throughout the year. (Tr. pp. 21-22)
18. Payment of the dues must be made within 30 days following the date of the statement that is mailed to each member. Members who are delinquent for a period of more than 120 days will be expelled from the membership rolls. (Taxpayer Ex. C)

19. Any member who is expelled may be reinstated upon payment of all past-due statements, a local reinstatement fee of \$50, and reinstatement charges, if any, imposed by the national office. All reinstatements are subject to approval by the Board. (Taxpayer Ex. C)

20. The taxpayer's policy on charitable contributions states in part as follows:

The monies raised through Club projects shall generally be earmarked as gifts and contributed to local Springfield social service organizations. \* \* \* All such contributions made by the Club shall be allocated on a needs basis determined by the Club's Board of Governors in consideration of the recommendations made to the Board by the Club's Charities Committee. (Taxpayer Ex. E)

21. The taxpayer's five guidelines for considering charitable requests include the following:

(1) The Club's charities money is contributed on a needs basis as determined by the Club's Charities Committee and approved by the Board of Governors.

(2) Contributions are made to not-for-profit social service organizations of Springfield who service the disabled, disadvantaged and those persons who are in need. Emphasis shall be placed on servicing youth needs first with funds available.

(3) Contributions are made for special requests and not for overall general operating budget expenses.

(4) Contributions are NOT generally made to governmental agencies (entities that receive tax supported funding) or religious funded organizations.

(5) Organizations which receive contributions through the Club for three consecutive years will generally NOT be eligible for consideration for the fourth year, unless the Committee determines the need merits consideration. (Taxpayer Ex. F)

22. The organizations that the taxpayer contributes to include the Boys and Girls Club, Boy Scouts, Girl Scouts, and Big Brothers Big Sisters, among other charitable organizations. (Taxpayer Ex. G)

23. For the fiscal year ending May 31, 2005, the taxpayer's revenue and expenses were as follows:

Revenue:

Membership dues	30,638
Less dues remitted to	
National	(15,692)
District	(3,067)
Big Hat <sup>2</sup>	(305)
Member events and functions <sup>3</sup>	37,420
Member donations	17,241
Special event revenue (less expenses of \$134,401)	121,879
Interest income	1,036

Expenses:

Program services	
Member events and functions <sup>4</sup>	31,310
Charitable contributions <sup>5</sup>	89,522
Supporting services	
Management and general	23,431
Fundraising	16,567
Interest Expense	57
Change in Net assets	\$28,263 (Taxpayer Ex. D)

24. The "Management and general" expense under the Supporting services for the fiscal year ending May 31, 2005 includes the following:

Accounting	\$5,985
Bad Debt	3,844
Board meetings	1,538
Officer stipends	7,800
Postage and printing	1,630
Seer—newsletter	2,634
Total	\$23,431 (Taxpayer Ex. D)

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<sup>2</sup> The "Big Hat Club" is composed of persons who have brought three new members into the club within a twelve month period. (Taxpayer Ex. C)

<sup>3</sup> This is the revenue received for lunches and social activities. (Tr. p. 26)

<sup>4</sup> This is the cost of the taxpayer's social functions. (Tr. p. 25)

<sup>5</sup> This is the money that the taxpayer disperses pursuant to its charitable policies and guidelines to benefit local charities. (Tr. pp. 11-12)

25. The “Fundraising” expense under the Supporting services for the fiscal year ending May 31, 2005 includes the following:

Advertising	\$262
Bank charges	804
Board member stipends	9,900
Gifts	308
Maintenance and repairs	417
Miscellaneous	1,888
Storage	700
Supplies	2,043
Telephone	245

Total \$16,567 (Taxpayer Ex. D)

26. The taxpayer is exempt from federal income tax under section 501(c)(3) of the Internal Revenue Code pursuant to a determination made by the Internal Revenue Service. (Taxpayer Ex. B1, B2)

**CONCLUSIONS OF LAW:**

The Use Tax Act (“Act”) (35 ILCS 105/1 *et seq.*) imposes a tax upon the privilege of using in Illinois tangible personal property purchased at retail from a retailer. 35 ILCS 105/3. Section 3-5(4) of the Act provides a list of tangible personal property that is exempt from the tax, and includes the following:

Personal property purchased by a governmental body, by a corporation, society, association, foundation, or institution organized and operated exclusively for charitable, religious, or educational purposes \*\*\*. On and after July 1, 1987, however, no entity otherwise eligible for this exemption shall make tax-free purchases unless it has an active exemption identification number issued by the Department. (35 ILCS 105/3-5(4))

Section 2-5(11) of the Retailers' Occupation Tax Act (35 ILCS 120/1 *et seq.*) contains a similar provision. (See 35 ILCS 120/2-5(11)).

The Department's initial tentative denial of the taxpayer's claim for an exemption identification number is presumed to be correct, and the taxpayer has the burden of

clearly and conclusively proving its entitlement to the exemption. See Wyndemere Retirement Community v. Department of Revenue, 274 Ill. App. 3d 455, 459 (2<sup>nd</sup> Dist. 1995); Clark Oil & Refining Corp. v. Johnson, 154 Ill. App. 3d 773, 783 (1st Dist. 1987). To prove its case, a taxpayer must present more than its testimony denying the Department's determination. Sprague v. Johnson, 195 Ill. App. 3d 798, 804 (4th Dist. 1990). The taxpayer must present sufficient documentary evidence to support its claim. *Id.* It is well-settled that tax exemption provisions are strictly construed and all doubts are resolved in favor of taxation. Heller v. Fergus Ford, Inc., 59 Ill. 2d 576, 579 (1975).

In order to determine whether the taxpayer is organized and operated exclusively for charitable purposes, the following factors are considered: (1) whether the benefits derived are for an indefinite number of people, persuading them to an educational or religious conviction, for their general welfare or in some way reducing the burdens of government; (2) whether the organization has no capital, capital stock or shareholders, and earns no profits or dividends; (3) whether the organization derives its funds mainly from public and private charity and holds them in trust for the objects and purposes expressed in its charter; (4) whether the organization dispenses charity to all who need and apply for it; (5) whether the organization does not provide gain or profit in a private sense to any person connected with it; (6) whether the organization does not place obstacles of any character in the way of those who need and would avail themselves of the charitable benefits it dispenses; and (7) whether the primary purpose of the organization, not any secondary or incidental purpose, is charitable. Methodist Old Peoples Home v. Korzen, 39 Ill. 2d 139, 156-57 (1968). These factors are balanced with an overall focus on whether and how the organization serves the public interest and



lessens the State's burden. See DuPage County Board of Review v. Joint Commission on Accreditation of Healthcare Organizations, 274 Ill. App. 3d 461, 468-469 (2<sup>nd</sup> Dist. 1995).

In the case of Rotary International v. Paschen, 14 Ill. 2d 480 (1958), which has facts similar to those in the present case, the Supreme Court found that the Rotary organization was not entitled to a charitable property tax exemption.<sup>6</sup> The court stated that Rotary's objective was "to encourage and foster the ideal of service as a basis of worthy enterprise," and while its aims were commendable, they were not charitable. Rotary International at 488. The court also found that Rotary's income was not derived from public or private charity because most of it was from per capita tax payments, registration fees, and interest. *Id.*

The same conclusion was reached in another case with similar facts, Kiwanis International v. Lorenz, 23 Ill. 2d 141 (1961). The Supreme Court noted that the Kiwanis clubs engaged in a variety of charitable, religious, and educational activities that included sponsoring Boy Scout and Girl Scout troops, sponsoring boys clubs, and conducting summer camps. The court found, however, that the Kiwanis clubs were formed by business and professional men "for exchanging experience, for fellowship, and to improve their leadership in the community." Kiwanis International at 146. The court stated that while the purposes were laudable and many of the activities of the local clubs were charitable, Kiwanis had other important purposes: the social, professional, and business advancement of its members. *Id.* The court concluded by stating that Kiwanis,

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<sup>6</sup> The factors that are considered in determining whether an organization qualifies for a charitable exemption from property tax are the same ones that are considered for charitable exemptions from retailers' occupation tax and use tax. See Wyndemere, *supra*.

like Rotary, does philanthropic work of public value, but each organization contains an element of personal advantage to their members. *Id.*

For the same reasons, it cannot be concluded that the taxpayer in the present case is a charitable organization. The taxpayer's objectives include fostering fellowship and cooperation among its members and other civic bodies and stimulating the desire of each member to be of service to their community. The taxpayer's bookkeeper testified that these goals are met through the social events where the members interact with one another. (Tr. p. 22) He stated that as a CPA, he found that being a member has been great for his business; the reason he joined the organization was for the opportunity to meet more people and take on new clients for his business. (Tr. p. 24) The taxpayer's primary purpose, therefore, is similar to the purpose of Rotary and Kiwanis, which is to promote the social and professional advancement of its members.

The taxpayer also has not met some of the other factors that are considered in determining whether an organization is charitable. Before becoming a member, a person must first be proposed by a current member and must pay dues that are never waived for those who are unable to pay. The failure to pay the dues results in expulsion from the club, and a member may be reinstated only upon payment of the amounts owed and a reinstatement fee. In addition, the taxpayer's income is not derived from public or private charity. Its income is primarily from membership dues, member events, and special events.

The taxpayer admits that it has other activities in addition to its charitable giving, but it contends that it is still organized for charitable purposes. The taxpayer's witnesses indicated that if an exemption identification number is granted, it would be used only for

the taxpayer's charitable purposes and would not be used at the member functions. The taxpayer claims that an exemption number would alleviate the need to pay tax on its purchases for the special events, but the taxpayer would not use the number for all of the club activities.

As previously mentioned, the Use Tax Act and the Retailers' Occupation Tax Act allow exemptions for institutions that are "organized and operated exclusively for charitable \* \* \* purposes." 35 ILCS 105/3-5(4); 120/2-5(11). The taxpayer has noted the case of Gas Research Institute v. Department of Revenue, 154 Ill. App. 3d 430 (1<sup>st</sup> Dist. 1987), which states that an exclusive charitable purpose does not need to be interpreted literally as the organization's sole purpose. Exclusive purpose is construed to mean the primary purpose and not merely an incidental or secondary purpose. Gas Research at 436. According to the findings of the Supreme Court in Rotary International, *supra.*, and Kiwanis International, *supra.*, entities that are organized and operated like this taxpayer are not organized and operated primarily for charitable purposes.

Because the taxpayer is not exclusively operated for charitable purposes and does not meet the requirement imposed by the statute, it is not entitled to an exemption identification number. As the Department indicated during the hearing, once an organization receives an exemption identification number, it is allowed to use it for all of its retail purchases. The statute does not allow an organization that is not primarily charitable to receive an exemption number for purchasing items related to any charitable activities that it conducts.

Recommendation:

For the foregoing reasons, it is recommended that the taxpayer's request for an exemption identification number be denied.

Linda Olivero  
Administrative Law Judge

Enter: January 10, 2007